

VZCZCXRO6533  
PP RUEHRG  
DE RUEHRI #0601/01 3051657  
ZNR UUUUU ZZH  
P 011657Z NOV 06  
FM AMCONSUL RIO DE JANEIRO  
TO RUEHC/SECSTATE WASHDC PRIORITY 3031  
INFO RUEHBR/AMEMBASSY BRASILIA 9453  
RUEHSO/AMCONSUL SAO PAULO 4367  
RUEHRG/AMCONSUL RECIFE 2723  
RUEHBU/AMEMBASSY BUENOS AIRES 0481  
RUEHMN/AMEMBASSY MONTEVIDEO 0320  
RUEHAC/AMEMBASSY ASUNCION 0330  
RUEHSG/AMEMBASSY SANTIAGO 0165  
RUEHOT/AMEMBASSY OTTAWA 0015  
RUEKJCS/SECDEF WASHINGTON DC  
RUCOMFA/HQ USSOUTHCOM J3 MIAMI FL  
RUEANHA/FAA NATIONAL HQ WASHINGTON DC  
RUEATRS/USDOT WASHDC

UNCLAS SECTION 01 OF 03 RIO DE JANEIRO 000601

SIPDIS

STATE PASS USTR:SCRONIN/MSULLIVAN  
USDOC FOR 3134/USFCS/OIO/WH/SHUPKA  
USDOC FOR 4332/ITA/MAC/WH/OLAC/JANDERSEN/ADRISCOLL/MWAR D  
STATE PASS OPIC FOR MORONESE, RIVERA, MERVENNE  
STATE PASS EXIM FOR NATALIE WEISS, COCONNER  
STATE PASS USTDA FOR AMCKINNEY  
AID/W FOR LAC/AA

SENSITIVE  
SIPDIS

E.O. 12958: N/A

TAGS: [ETRD](#) [FAIR](#) [MARR](#) [BEXP](#) [BR](#)

SUBJECT: BRAZIL'S EMBRAER: SEEKING A U.S. DEFENSE RUNWAY FROM  
WHICH TO SOAR

¶1. (U) Summary: On October 21 Admiral Edmund P. Giambastiani Jr., Vice Chairman of the Joint Chiefs of Staff, the Ambassador, and the Consul General met with Embraer President & CEO Mauricio Novis Botelho and Executive Vice President for Defense and Government Market, Luiz Carlos Aguiar, to review bilateral commercial relations between the U.S. and Brazil. Our Brazilian interlocutors discussed Embraer's recent history and strong financial status, the company's success in the regional and executive jet markets, and its desire to continue doing business with the U.S., particularly in the defense "niche market." Admiral Giambastiani emphasized the USG's need for joint service platforms that maximize military utility and cost efficiency. End summary.

#### EMBRAER'S POSITIVE RISK PROFILE

¶2. (U) Embraer's Botelho said he thought it would be fruitful to talk about the benefits that both countries can gain with increased partnership. He started out by focusing on Embraer's positive financial status and risk profile, stating that he feels that Embraer is a "good example of what free trade is all about," with US 20 billion dollars in exports last year and 10 billion dollars in imports. 12 to 14 billion dollars worth of goods and services were exported just to the US. Those statistics put Embraer just behind Airbus (France) and Boeing (US) in the aircraft market, and vying for third place with Bombardier (Canada). Botelho indicated that Bombardier is technically bigger in terms of overall revenue, but that Embraer has surpassed Bombardier in commercial aircraft. Embraer represents approximately 50 percent market share at present in 36 to 126-passenger aircraft.

¶3. (U) Operating in 69 countries, the company enjoys excellent financial status and recently received an investment grade rating by both Standard and Poors and Moody's. The company has a nearly US 14 billion dollar backlog of solid orders and an additional almost 15 billion dollars in options, totaling more than 2,000 aircraft, and it has been ranked as one of the largest Brazilian exporters since 1997. It is a major player on commercial aircraft, and has a niche operation in the defense market. In the U.S., Embraer has

facilities located in Ft. Lauderdale and in Nashville. In addition, it recently announced that it will establish facilities in New Hartford, CT and an additional one in Ft. Lauderdale, as well as one in Mesa, Arizona which will potentially employ 250 workers. Currently, Embraer has 38 additional service centers to sustain its fleet of business jets.

¶4. (U) Embraer has developed risk-sharing partnerships with major U.S. aerospace companies, including General Electric Engine Company, Allison Engines (later purchased by RR), Honeywell, Hamilton Sundstrand, C&D, and Goodrich. It also has relationships with suppliers distributed among 25 U.S. states, and estimates that more than 7,000 U.S. jobs were either created or maintained in 2005 from a component purchase. More than 1200 aircraft have been sold to the U.S., including 345 turboprops and about 800 jets. Airline customers include American Eagle, Continental Express, Republic Airways, Midwest, Tran States, Mesa, Gecas, US Airways, and Jet Blue. Botelho characterized the 70-80, 100, and 126-seat jets as "small big jets", saying they really don't meet the criteria of regional jets anymore given their passenger capacity and comfort.

#### INVESTMENT IN THE FUTURE AND "PROTECTING THE CAMP"

¶5. (U) According to Botelho, the history of Embraer shows a successful evolution from a state-owned enterprise to privately held corporation. State-owned until December, 1994, it was privatized in 1995, when current management took control. In 1997, it reached break-even in terms of profitability, and since then has steadily grown. Embraer employs 19,000 employees worldwide, including 3,000 outside of Brazil, and has more than 4,000 engineers. From 2001 to 2005, about 540 engineers graduated with master's degrees specializing in aeronautical engineering, all paid for by Embraer. As Botelho says, "it's a business based on knowledge." The

RIO DE JAN 00000601 002 OF 003

Ambassador complimented Botelho on training some of the world's best engineers and observed that Embraer is currently suing Gulfstream for recruiting some of them away. Botelho said, laughing, "the Admiral will understand this. We have to protect our camp."

¶6. (U) Adm. Giambastiani acknowledged that skilled people are in tremendous demand, and asked what had brought Embraer to the decision to provide the training. Botelho said that they had analyzed the situation and realized there was not enough flow in Brazilian universities to supply the demand. It was not the level or quality of education available; Embraer's parastatal parent was created in the 1950s, and its first dean had previously been the head of the aeronautics department at MIT, so it was created with the same curriculum and standards. "But," said Botelho, "Competition is heavy. The investment banking sector takes a lot of our engineers away. . . it is really our biggest competitor."

#### COMPANY STRUCTURE

¶7. (U) Embraer restricts voting power to five percent for any shareholder, and limits foreign ownership to that of 2/3 of the Brazilian shareholders. Botelho indicated that if any shareholder reached 35 percent, Embraer would be forced to open the company to a 100 percent public offering. The GOB retains one voting share, to assure veto power on such proposals as new military programs, transfer of technology to other countries, changes in the bylaws, and the ability of someone else to purchase the company. However, said Botelho, even if a prospective buyer could achieve government buy-in, the company is further protected: the prospective buyer has to meet an asking price that is the value of the company plus 50 percent. As Botelho said, "That makes it less attractive." Embraer shares are traded on the NYSE and Sao Paulo Stock Exchange at 60 percent and 40 percent of its shares, respectively-further protection through market diversification.

#### FROM CORPORATE JETS . . .

¶8. (U) The Ambassador turned the conversation to small, private business jets. Botelho said that five years ago, Embraer launched the Legacy aircraft, with the intent to understand and learn how the market for small, executive jets works. They "learned a lot," and

the Legacy-600 was born. From there, they launched a couple of new product lines with specialized or niche markets. They do not plan to build large numbers of these craft, but the intent is to "show the market that they are following demand." They are also competing effectively with larger and/or more expensive aircraft in terms of comfort and features offered; Legacy aircraft are being very well received, with about 320 orders so far, projected to be ready in two tranches in mid-2008 and mid-2009. The executive jet market is growing, and Botelho believes it will keep growing. As for defense, he sees that as a "niche operation, with some opportunities."

#### TO POSSIBLE DEFENSE SALES TO THE USG

¶9. (SBU) The Admiral stated that while he does not negotiate contracts, he would be happy to respond to Embraer's questions regarding the direction in which the US is moving, in particular with respect to intelligence, reconnaissance and surveillance (ISR) aerial manned platforms. Adm. Giambastiani explained to Embraer President Botelho and Vice President Aguiar that he is co-chairman of the USG's Defense Acquisition Board and that all programs for acquisition go through the Board. While there are a variety of other mechanisms within OSD for contract solicitation, no programs can go through without the Board's approval.

¶10. (SBU) Botelho said that Embraer looks at the defense market not so much as competing with U.S. firms, but complementing U.S. partners in competing for defense work. The reliability of its originally proposed Aerial Common Sensor (ACS) aircraft [E-145] is estimated at 99.75 percent. With prime contractor Lockheed Martin, Embraer had been contracted to deliver 38 aircraft for the US Army,

RIO DE JAN 00000601 003 OF 003

and 19 aircraft for the US Navy, with deliveries anticipated from 2009 to 2017. The contract was awarded in August 2004 and terminated in Jan. 2006. Botelho said that by the time the contract was awarded, the ACS platform complied in total with stated requirements, but when the program became Joint with the Navy and requirements grew, it became evident that the E-145 could not meet the increased weight, power and cooling requirements. Embraer worked rapidly and flexibly to offer the larger E-190 instead, but it was not feasible to effect the mission payload integration within the costs of the program and the contract was terminated by the Army. It "would have been a big hit for Embraer to serve the U.S. government and to open new opportunities abroad," Botelho said ruefully. As he put it, "Our situation today is that we have the conditions to keep supplying value. Where and how are the questions. I honestly do not know if there is additional opportunity, and would like to hear from the U.S."

¶12. (SBU) The Admiral noted that a series of studies was commissioned in the U.S. as to whether manned or unmanned platforms would meet future military requirements. Unmanned platforms do not meet all those needs, so there will be a program for a manned ISR platform. However, the program will be Joint from its inception, incorporating all Army and Navy needs up front. He said, "You will see the U.S. come back in for solicitations and bids in 2007," cautioning once again that he does not handle that, but will be reviewing requirements and cost drivers. But as he said, "We are serious about the program. But it must be a joint program, a joint operation, and a common platform." The Admiral stressed that the U.S. military's focus for the future would be capability, reliability, and cost effectiveness, including examining long-term life cycle costs and energy efficiency. Botelho closed by saying "We will compete strongly!"

¶13. (U) This cable was cleared by Ambassador Sobel and Admiral Giambastiani's staff.

Martinez